EL PASO ELECTRIC CO

Moderator: Steven P. Busser
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8:00 am CT

Operator: Good day, everyone and welcome to the El Paso Electric Company 4th Quarter 2012 Earnings conference call. Today's call is being recorded. At this time, I would like to turn the conference over to Mr. Steven Busser.

Steven Busser: Thank you, Dana and good morning to everyone. Welcome to the El Paso Electric Company 4th Quarter 2012 Earnings conference call and Analyst Day. My name is Steve Busser, and I am the Treasurer for El Paso Electric. Before we get started, I'd like to go over some items and then introduce our panel.

Before I go over the Safe Harbor on the second slide, I'll cover some items. We will file our 10-K with the SEC on or before February 28, 2013. As for upcoming Investor Relations events, we plan to be at the Sidoti Conference here at the Grand Hyatt on March 18 and March 19, 2013 and we'll also be going on a sell side marketing tour with Ladenburg Thalmann on March 20 and March 21, 2013.

Moving to the Safe Harbor statement, in summary, our comments and answers to your questions may include forward-looking statements made pursuit to the Safe Harbor Provisions of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks and other factors, which may cause the Company's actual results in future periods to differ materially from those expressed here. Any such statement is qualified by reference to the risks and factors discussed in the Company's SEC Act filings.

Our 10-K and other SEC filings contain our forward-looking statements and also lay out the risk factors that should be considered. These filings may be obtained upon request of the company on our website or from the SEC. The Company cautions that the risk factors discussed in these filings are not exclusive and we do not undertake to update any forward-looking statement that may be made from time to time, by and on behalf of the Company.

These statements, especially those made during the question and answer section of the call are subject to risks and uncertainties that are difficult to predict. Moving to slide 3, I'd like to introduce our Executive Management team and our guest speaker. Our first speaker today will be our CEO, Tom Shockley, who will cover the 2012 highlights, 2013 goals and an outlook for El Paso.

Tom has been our permanent CEO since May of 2012 and served as a member of our Board of Directors since 2010. Tom brings over 35 years of experience in the utility industry to El Paso Electric and was formerly Vice Chairman and Chief Operating Officer at American Electric Power Company.

Bill Gilmer is our guest speaker today. Bill is the Director of the Institute for the Regional Forecasting at University of Houston's Bauer College. Before joining the Institute, Bill worked for the Federal Reserve Bank of Dallas for 23 years, retiring from the Bank as a Senior Economist and Vice President. Bill served the Federal Reserve Bank of Dallas as the Officer in charge of the El Paso Branch from 2003 to 2012, where he oversaw the bank's operations in West Texas and New Mexico.

Bill holds an MA and Ph.D. in Economics from the University of Texas at Austin. Bill's work on the Texas economy has been recognized by publications such as The Wall Street Journal, The Economist and Forbes. Bill will provide an overview of the El Paso economy during the call. Then he will go in more in-depth presentation of the El Paso economy after the question and answer session of our call today.

We also have with us today, our Chief Financial Officer, David Carpenter, who will review the 2012 earnings, our capital construction program and our 2013 guidance. David has served as our CFO since August of 2009 and has more than 35 years of experience in the electric utility industry. Before I turn the call over to Tom, I also wanted to introduce Lisa Budtke who is here with us today. Lisa is our Assistant Treasurer and Richard Gonzalez, who was recently promoted to Supervisor of Investor Relations. He has been an instrumental part of the Treasury team and the Investor Relations functions for the last several years. He is going to be the main point of contact from an Investor Relations perspective with the Company going forward. Now, I'd like to turn the call over to Tom.

Tom Shockley: Thank you, Steve. Let me first of all welcome all of you here and tell you how much we appreciate you being here. We will try to step through this information and give you a little bit of insight into what the highlights were in 2012 and what we're then going to be focusing on in 2013, and then a little bit of look of what's happening in El Paso.

In 2012 we had a number of different financial activities that really strengthened the Company. Early in the year the Revolving Credit Facility was increased from $200 million to $300 million. We then took advantage of the low interest rate environment and refinanced almost $100 million of Pollution Control Bonds.

Then late in the year we issued some senior debt at a very, very attractive 3.3 percent. Other things that happened during the year that we are very pleased about and I don't know if all of you remember we were involved in a very contentious rate case with the City and subsequently the Public Utility Commission of Texas (PUC) and we were able to settle that in April 2012. And I can tell you that the relationship with El Paso Electric and the City have improved substantially. So we are very, very pleased about that.

Also, late in the year we had the opportunity to add two new local Directors to our Board. Ed Escudero was one of the individuals added and Woody Hunt was the other one. Both are very prominent businessmen in El Paso and we could not be more pleased at having them join our Board.

Our five-year growth pattern has been pretty stellar and we are proud of that. I think you've got a chart that will show that and it also points out the fact that we really survived through the major dip in the economy in a way that a lot of other areas in the United States were not able to.

As far as achievements we were able to achieve in the operations area, I would like to tell you how proud we are that with regard to interruptions, which is something that the PUC of Texas tracks, this is our second year in a row that we were first in interruptions duration and first in interruption frequency, and so we are very, very pleased at that.

Palo Verde has turned in another stellar year for 2012 as well. For next year, we are going to be focusing on finishing up our first aero-derivative 87 megawatt gas turbine peaker. And it will be coming online in May of this year. It will give us a lot of flexibility of being able to follow load which is one of the real challenges that we have in El Paso because we're getting a substantial amount of solar. And these units that we are installing, finishing this year and then in the years to come will give us the flexibility of being able to track the load very quickly and efficiently.

We will also be getting the permits that we need for our new station that will be built in East El Paso. It's the area that is very, very rapidly growing and we've got a plan - a long range plan that will see four new peaker units on that particular site. The other activities we'll be involved in this year is to focus on a successful conclusion of the negotiations with our unions that will start later this year and be in place with the new contract in September.

And then finally, as we spend this new capital going into service for our customers we'll require increased rates from our customers and that will be something that we will start working on with regard to making sure there's no surprises, identifying when it will be happening and making everyone aware of what our expectations are and moving down that road in preparation. The outlook for El Paso is really exciting. I think in your handout you will see a number of different projects in different places that will give you a little bit of insight as to why we feel like El Paso is a really great place to be and a great place to have the electric franchise.

Things are happening on the base. Things are happening in our medical community, in our research community, and there's just a whole lot activity. And stepping on through these, one of the most exciting things that came to be in November of last year, was the City voting on a Quality-of-Life bond that will provide, over the next ten years, $474 million for improvements to the city, such as swimming pools, parks, recreational areas and things that truly will enhance the quality of life.

In addition to that, the City Council also approved the construction of a downtown Triple-A ball park that will completely revitalize the downtown area and we think, just convert El Paso into one of the best places that you can be. We will have a Triple-A ball team coming in.

A group of investors have arranged to bring what was the Tucson Padres into El Paso, and we're excited about that. So you're going to get a lot more information this morning about the economy and things happening, but El Paso is a great place. And with that, I'd like to turn it over to Dr. Gilmer.

Bill Gilmer: Thank you Tom. To give you a quick overview of some of the economic things that are happening in El Paso, this is the payroll jobs. This is seasonally adjusted data from the Federal Reserve Bank of Dallas.

And this employment data also includes many of the revisions the Dallas Bank benchmarks continuously, and so you'll see many of the revisions that we'll see later this month in metropolitan data are already included here. What you see is the continuation of the recovery in El Paso through 2012, and a slowdown in the second half of 2012, the tapering off of growth.

The 2013 forecast for El Paso is sort of a mirror image of this with expected relatively slow growth for the first half and then it'll pick up in the second half of the year. The local slowdown in 2012 really just follows what we saw in the national economy where we had a good reading on GDP (Gross Domestic Product). It just turned out that in the third quarter of the year, that reading on GDP, much of it was inventory accumulation and it forced the significant cutback in production in the last quarter of the year.

The other part of the slowdown, also very visible in GDP statistics and which almost certainly was felt in El Paso, is the threatened sequester of $109 billion in federal spending, half of which would come in military budgets. The military has clearly been planning for the worst, slowing spending in advance of any actual event, should that occur.

I will come back to the sequester in a minute. But let's just put it aside for just a moment and talk about the planned expansion of Fort Bliss and how Fort Bliss is expected to continue to provide some significant stimulus, continued stimulus to the local economy. This is the last year of the planned build out of Fort Bliss. This will be the fourth year in a row that we are spending $500 million in continued construction on the base.

The arrival of troops and their families continues in 2013. We are still expecting about 8,800 new residents, spouses and children included. This expansion brings considerably different kind of stimulus than the construction program. This brings continued spending on autos, retail housing to the city and the entire 50,000 increase in population on the base.

Just that increase on population on the base is through the entire construction program, it represents about a 6 percent increase in population in El Paso. We already mentioned the William Beaumont Medical Center, the construction contract for that was awarded in late January, the Triple-A Baseball stadium and the other kinds of construction stimulus that is now planned for the coming future.

If you look at the outlook for the US economy broadly, from something like the Blue Chip Survey or, the Survey of Professional Economists, again, it's relatively weak first half scenario primarily due to fiscal drag from $200 billion in taxes. All expectations are that that's overcome as we move through the year by strengthening the underlying national economy. And risk to the national economy comes that we perhaps underestimated the drag from the $200 billion in taxes already in place, that we impose significant new drag through the sequester process, or that we've simply under estimated the drag that could arise.

But, as I said, by the second half we expect to see a pick up and to move into some growth rates near 3 percent by early 2014. El Paso again should follow this trend but, it has additional advantages that extend just beyond the military expansion.

A key part of US growth this year is expected to be in the housing market. We're expected to finally see housing begin to add small amount to US GDP. The housing recovery in El Paso is considerably more advanced than what we have seen in the US. We've seen a sharp upturn in housing prices in El Paso and in home sales.

I think as a relatively poor community, El Paso would benefit significantly from the new definition of a qualifying mortgage from the Consumer of Protection Agency, which is really going to give bankers a map going forward on how they can lend to a relatively high risk community, like you might find in El Paso. Mexico continues to be on a very strong growth path. The growth expected to be 3 to 4 percent and I think as the risks to the global economy recede, as we move past the recession in Europe, and as we begin to see emerging economies, particularly China begin to accelerate over the course of 2013 from their slow down last year, this benefits the Peso.

And as the Peso strengthens, that helps retail trade in El Paso and Mexico maintains a privileged place in the rationalization of manufacturing in North America after NAFTA. Despite the slowdown in manufacturing in the last quarter of last year, we have seen continued growth in Maquiladora employment and see that what its estimates from the Federal Reserve Bank of Dallas are that it continues to grow at about a 5 percent rate. And trade through the movement of goods through the port of entry in El Paso will continue to grow at about a 6 percent rate through November of this year. So cross border trade still a plus for El Paso.

Payroll job growth in El Paso should easily match the 1.4 percent growth of last year. Tom Fullerton at the University of Texas El Paso (UTEP) is forecasting a 1.9 percent increase for the year. Roberto Coronado at the Federal Reserve Bank of Dallas is forecasting about a 1.5 to 2 percent gain in employment for El Paso.

The risk of sequester, risk from the physical negotiations, the risks are really not particularly well understood. We do have a memo from the Secretary of the Army that was dated early this year. This memo basically outlined actions that should be taken immediately from a hiring freeze to cuts in spending.

Construction was really not specifically mentioned and neither was the planned relocation of military personnel, the two factors that would most impact the current program at El Paso. You see here outlined the civilian hiring freeze, the termination of temporary employees, curtailment of non-combat training, cutting of maintenance studies, R&D overseas moves of civilian employees, and an order to act immediately to avoid not having acted before the sequester, might be put in place.

It’s interesting that the Army did allow, in late January, the contract to be let for the new medical center, the William Beaumont Medical Center, in late January by the Corps of Engineers, so construction projects are apparently continuing to move forward, at least at this time. Thank you very much.

David Carpenter: Good morning. Thank you, Bill. Now we're going to move on and talk about our fourth quarter earnings results for the comparison of 2012 versus 2011 fourth quarter year-to-date earnings results is summarized on this slide. As you can see, fourth quarter 2012 basic earnings per share was $0.12 per share, which is a slight decrease from the $0.14 per share that was earned in the fourth quarter of 2011. For the year-to-date period, earnings were $2.27 per basic share. This compares to the year-to-date earnings in 2011 of $2.49 per basic share.

We will provide additional detail on the next two slides, on the factors that have been affecting earnings. On slide 24 for the fourth quarter of 2012, we reported net income of $4.8 million, or $0.12 per basic share, compared to the fourth quarter 2011 net income of $5.5 million, or $0.14 per basic share. Positive earnings drivers include increased earnings of $0.04 per basic share for the Allowance for Funds Used during Construction, or AFUDC.

The construction of Rio Grande Unit 9 and the Montana Power Station, which in Rio Grande Unit 9 is scheduled to come online in May of this year, are the primary factors which have increased the capitalization of AFUDC. Decreased non-Palo Verde operations and maintenance expense largely due to the resolution of a Public Service Company of New Mexico, Transmission Rate Case, resulted in a decline in transmission expense for purchased transmission with no comparable activity in the fourth quarter of 2011, and was primarily responsible for a $0.04 increase in earnings per share in the fourth quarter of 2012.

On the negative side, we saw a $0.06 decline in basic earnings per share due to a decrease in retail non-fuel based revenues, due to the reduction in our rates from the Texas Rate Settlement and milder winter weather. We also had a negative impact of $0.05 per share for other, which are several minor items, none of which are significant.

On slide 25, for the 12 months ended December 31, 2012, we posted net income of $90.8 million, or $2.27 per basic share compared to net income of $103.5 million, or $2.49 per basic share for the 12 months ended December 31, 2011. Earnings for the 12 months ended December 31, 2012 were positively affected by decreased depreciation and amortization expense, increasing earnings per share by approximately $0.05 in 2012, which reflects the approval of the license extension for Palo Verde in 2011, and the reduction of transmission and distribution, and gas bar generation depreciation expenses in 2012, as a result of the Texas Rate Case settlement.

Higher allowance for funds used during construction due to the higher construction work in progress balances also contributed $0.04 to the increase in earnings per share. The largest positive driver to earnings per share for the 12 months ended December 31, 2012 compared to the same period in 2011 was an $0.08 pickup due to the share repurchases that occurred in 2011. Once again, much like the quarterly earnings drivers, reductions in retail non-fuel based revenues accounted for a $0.16 per share decrease in earnings per share, due to the Texas Rate Case Settlement and milder weather than 2011.

Earnings were also negatively impacted by $0.11 per basic share due to increased non-Palo Verde operation and maintenance expense. Increased operation and maintenance expense was primarily due to increased employee pensions and benefits expense reflecting lower discount rates, used to determine post-retirement benefit cost. Also during 2012, we have seen a reduction in deregulated Palo Verde Unit 3 revenues we collect from New Mexico customers, which reduced our earnings per basic share by $0.08.

This is primarily the result of lower gas prices, which have resulted in lower proxy prices for power provided by Unit 3. Decreased transmission revenues contributed to a $0.04 reduction in earnings per share in 2012, as compared to 2011. The reduction is attributable to a settlement agreement with Tucson Electric Power Company that resulted in one-time income of $3.9 million pre-tax in the third quarter of 2011.

On slide 26, we show changes in revenues and sales. Overall, retail non-fuel based revenues decreased $3.7 million pre-tax, or 3.1 percent in the fourth quarter of 2012, compared to the same period in 2011. This was due to a reduction in non-fuel based revenues to our Texas customers, which became effective May 1, 2012.

Commercial and industrial customers were primarily impacted by the change in revenues. As you can see, non-fuel based revenues for small commercial and industrial customers and large commercial and industrial customers decreased by 5.3 percent and 9.4 percent in the fourth quarter of 2012, compared to the fourth quarter of 2011. Kilowatt hour sales to residential customers also decreased by 2.8 percent for revenues, due to a 3.6 percent reduction in revenues in kilowatt hour sales reflecting milder winter weather in the fourth quarter of 2012.

For the year-to-date period, 2012 retail non-fuel based revenues decreased by $9.7 million pre-tax, or 1.7 percent compared to the same period in 2011. The decrease in revenue was also due to the reduction in non-fuel based rates to our Texas customers, which primarily impacted the commercial and industrial customers. Non-fuel based revenues from sales to small commercial and industrial customers and large commercial and industrial customers decreased 4.1 percent and 7.1 percent, respectively.

In addition, large commercial and industrial revenues decreased as a result of several customers moving to lower interruptible rates during 2012. Kilowatt hour sales to residential customers increased 0.6 percent in the 2012 period compared to the 2011 period, due to a 1.4 percent increase in the average number of customers served. During the 12 months ended December 31, 2012, cooling degree days decreased 8.3 percent when compared to the same period in 2011, but were 9.2 percent above the ten-year average.

Heating degree days decreased 16.4 percent during the 12 months ended December 31, 2012, when compared to the same period in 2011 and was 9.8 percent below the ten-year average. Kilowatt hour sales to public authorities still increased 2.4 percent and non-fuel based revenues increased 1.9 percent.

On slide 27, we show the impacts of the rate decrease in weather on non-fuel based revenues for the fourth quarter and year-to-date periods in 2012 compared to the same periods in 2011. As you can see, the Texas Rate Case Settlement had a $3.3 million negative impact in the fourth quarter and $11.7 million negative impact on the year-to-date period. We will see an additional $3.3 million negative impact in 2013.

As previously discussed, weather had a significant impact on 2012 compared to 2011, with a $2.7 million impact in the fourth quarter and a $9.7 million negative impact year-to-date. The impact of weather, compared to the ten-year average, was still a positive $2.2 million. Excluding the rate decrease and weather, we saw an increase in revenues of 1.8 percent in the fourth quarter and 2.1 percent in the year-to-date period, reflecting the continued growth in our service territory.

On slide 28, in 2012; our primary capital requirements were for construction and purchase of an electric utility plant, nuclear fuel purchases and the payment of common stock dividends. As you can see, we spent approximately $202 million on a new electric plant. In addition, we paid approximately $39 million in dividends to shareholders.

In December 2012, we issued $150 million of ten-year unsecured senior notes at a coupon rate of 3.3 percent, the proceeds of which were used to repay our outstanding balance of Revolving Credit Facility and to fund capital construction program in 2013. As a result, we had a cash balance of $111.1 million at December 31, 2012. We also had liquidity of approximately $388 million, including cash and the Revolving Credit Facility at December 31, 2012.

In summary, we believe that we are well positioned to finance our construction program in 2013 and later years. Now, turning to our capital construction program, on slide 30, this chart shows our expected capital expenditures for construction over the next five years. We plan to spend $264 million on cash construction expenditures in 2013, and anticipate increasing that amount to $326 million in 2014.

Our cash construction expenditures will be in the $200 million range for the last three years of the five-year period. Our five-year estimated capital expenditures total $1.2 billion, which includes the addition of the new Montana Power Plant. Our capital expenditures ensure that we have the generation capacity to meet our customers' growing demand for electricity, and includes expanding and updating our transmission and distribution infrastructure.

The increase in expenditures in 2012 and 2013 reflect a new expected in-service date for the first Montana unit in the fourth quarter of 2014. Our generation expansion plan is shown on the next slide. On this slide, we show our expected generation additions and total capacity compared to our forecasted peak demand for each year during the 2013 to 2017 period.

Our current generating capacity is approximately 1,765 megawatts, and is projected to grow steadily through 2017. Our current cash construction program calls for the completion of construction associated with Rio Grande Unit 9 and the commencement of operation in May of this year. The construction program also provides for the addition of four new aero- derivative peaking units of 88 megawatts each over a four-year period spanning 2014 to 2017.

During this period, one unit per year will be placed into service at the new Montana Power Station on El Paso's East Side. The first unit is expected to be completed in the fourth quarter of 2014. It is also important to note that some of our current units will be retired during this period. Our current plan is to retire Rio Grande Unit 6 in 2014, and to retire or sell our stake in the Four Corners Generating Units 4 and 5 in 2016.

On slide 32, we show generation capital expenditures are anticipated to total approximately $572 million through the next five years. The bulk of these capital expenditures, approximately $325 million, will be invested in new generating plant. Approximately $166 million will be for capital improvements and replacements at Palo Verde, and other generation totals $81 million. Compared to our 2012 capital expenditure plan, we have moved up the peaking units and pushed back the addition of a base load combined cycle unit to better match our load profile.

On slide 33, transmission and distribution capital expenditures are expected to be approximately $488 million through 2017. Approximately $176 million has been earmarked for transmission projects, the majority of which are related to reliability and system expansion activities. $312 million is projected to be spent through 2017 on distribution projects, which are primarily for expanding the distribution system to serve customer growth.

Turning to slide 34, general plant is expected to increase by $140 million over the next five years, including capital expenditures to construct two new distribution centers that will consolidate facilities to make our operations more efficient. The first distribution center will be built on 50 acres next to the new Montana plant site, and will be operating with a base of about 235 employees.

On this slide, we detail projected rate base at the time new generation plant additions for each year from 2013 to 2017. The beginning rate base balances shown here include the deregulated portion of Palo Verde Unit 3. As you can see, plant additions are estimated to be approximately $279 million per year through 2017.

The total rate base will be decreased by the accrual and recovery of depreciation and increases in accumulated deferred income taxes. We expect that total rate base to grow to nearly 2.4 billion at the time the last Montana Power Station unit is placed in service. This slide anticipates the best timeline projection for filing our next rate case with the Public Utility Commission of Texas.

Due to the delay in the completion date for the first unit of the Montana Power Station, we think that we can delay filing a rate case until 2015, although a final decision has not been made. The primary reason for delaying a rate case filing until 2015 is to reflect the first unit of the Montana Power Station and common cost, which will be higher up front into rate base along with the increased operating cost for a new Greenfield plant site.

Now moving to earnings guidance for 2013 - on slide 38, we are initiating our 2013 earnings guidance at $2.20 per share to $2.60 per share. This diagram shows actual 2012 earnings per share of $2.27, compared to the midpoint of our projected 2013 earnings guidance of $2.40. As you can see, 2013 projected earnings are expected to be negatively impacted by increased depreciation and amortization related to increased levels of depreciable plant in 2013, which will reduce earnings by approximately $0.07 per share.

Higher interest expense primarily related to the $150 million of senior notes issued in December are expected to reduce earnings by approximately $0.06 per share in 2013. However, this will be offset by the accrual of higher amounts of allowance for funds used during construction reflecting our higher construction work in progress balances of approximately $0.10 per share.

Lower non-fuel based revenues related to the Texas Rate Case settlement are expected to lower earnings by $0.06 per share and we expect operation and maintenance expenses in 2013 to only increase by about half a percent which would lower earnings per share by about $0.02 per share. On other items that are expected to increase our 2013 earnings per share include increased deregulated Palo Verde Unit 3 revenues and other off-system sales revenues due primarily to higher expected natural gas prices. And also increased revenues to reflect the continuing growth in our service territory will result in an increase in earnings per share estimated at $0.18 per share resulting in a midpoint of earnings guidance of $2.40 per share.

The primary factors that will affect the range of $2.20 per share to $2.40 per share include the variability in revenues associated with weather impacts in our service territory. It also includes potential variances in operations in maintenance expenses both for Palo Verde and our other operations. And then it also includes - the other primary factor is variations in the amount of revenues that we receive from our deregulated portion of Palo Verde Unit 3 in New Mexico, which is primarily influenced by natural gas prices.

With that, I'm going to turn the call back over the Steve Busser to take questions and answers.

Steve Busser: Thank you, David. So at this point we'll take questions and answers, and just to make sure that we have some order to the process, what we'll do is we'll go ahead and take the questions for the folks that are in the room first and then we'll move to the folks who are on the call who may have questions. Once we get done with the Q&A session, we're going to turn it back over to Dr. Gilmer for a more in depth presentation on the El Paso economy and the drivers there.

So, without further ado, if there are any questions in the room, just go ahead and raise your hand. I would just ask that you state your name before you state your question and Lisa will bring you a microphone.

Neil Mehta: Neil Mehta, Goldman Sachs. A quick question here on AFUDC, it looks like from the waterfall the AFUDC provides a $0.10 pick-up in 2013. How do you think about AFUDC in 2014 and 2015? CAPEX ticks up in 2014, so shall we think AFUDC's year-over-year contribution will increase as well?

David Carpenter: Yes, Neil, this is David Carpenter the allowance for funds used during construction is going to vary as you state, as we spend additional money on capital expenditures. So, in 2013, we will close the Rio Grande plant which will bring our CWIP balance down, but that's more than offset by the Montana Power Station expenditures which then result in a net increase in 2013.

Then in 2014 the first unit of the Montana plant is not expected to be completed until late in the year and so I would expect AFUDC to increase in 2014 and then once the Montana plant is completed in late 2014 and then the second unit in May 2015, we would expect to see a drop off in 2015.

Neil Mehta: Got it. And some cash flow questions here. What can you talk through your dividend growth strategy? You've got a below average dividend payout, but you also have a heavy CAPEX program and less headroom from an equity-to-cap perspective.

David Carpenter: Well, I think what we've stated is that we've been targeting a 45 percent payout ratio and I think that we will continue to see that for the next several years. I think as you look at our construction program here, through 2015 we have a fairly heavy construction program and so I would expect that our dividend policy would be fairly consistent through that period and then once you get through that heavy construction period will probably be the time we take a second look at the policy.

Brian Russo: Yes, could you remind us what the AFUDC rate is?

David Carpenter: Yes, the AFUDC rate is approximately 8.5 percent.

Brian Russo: Okay.

David Carpenter: That's debt and equity.

Brian Russo: And the goal of the net plant hitting the income statement in 2013 and beyond - what leverage do you guys have in terms of managing your O&M to help preserve your earned returns until the next rate case?

David Carpenter: Well, we try to operate as efficiently as we can all the time. I think that the one expense that hit us harder in 2012 was our pensions and benefits expense and we're continually monitoring our assumptions for recording pensions and retiree benefits. We also are looking at our compensation programs, including our benefits and are trying to set programs up that are both efficient from a cost standpoint and also provide benefits to retain and attract employees.

So we'll continue to do that and we'll continue to try to manage our operations as efficiently as possible to manage our expenses. At this time we don't expect any layoffs or anything more drastic as far as operation and maintenance expenses.

Maury May: Good morning. Maury May, Wellington Shields. Question on the rate cases. You're going to file in Texas in 2015 based upon a historic 2014 test year, but what about New Mexico, because they've got that forecast test year?

David Carpenter: We're in a little different position in New Mexico. We haven't had as much load growth in New Mexico. Most of it has been in Texas the last year or two and so we potentially would put off filing a rate case in New Mexico until after 2015. We'll just kind of continue to monitor how the load growth between Texas and New Mexico occurs, but right now most of the load growth is in Texas and so that's where the rates are under recovery.

Maury May: So, most of the investment in Rio Grande 9 and Montana 1 are going to go to the Texas rate base?

David Carpenter: Most of them will go at the Texas rate base.

Maury May: So, it's not a 75/25 split?

David Carpenter: Not at this time.

Maury May: Okay. And my second question has to do with, capital expenditures. Can you just give us some detail here? Rio Grande 9, can you review the price tag on that one and also on Montana Unit 1, the price tag for that unit plus the common facilities you've got to build to get that one up to.

David Carpenter: Steve's looking up the Montana plant. Rio Grande 9 is going to come in running a little bit over budget and is going to come in about $91 million is the expectation. On the Montana Units...

Steve Busser: More the cost of the Montana units are a little bit difficult to parse them out individually, but the first unit that will come online in Montana will be about in the $71 million range. But then in addition to that, there will be north of $50 million worth of additional common costs that are in place that will come in the rate base at the time we put that first unit into service. And then beyond that, each unit will be in the $65 million to $70 million in terms of cash expenditure. The numbers that I just gave you were cash expenditures excluding AFUDC.

Anthony Crowdell: Good morning. Anthony Crowdell, Jefferies. I just want to follow up on Neil's question, it seemed that, I guess, AFUDC in 2014 will increase relative to 2013, but is that more than enough to offset, I guess, any higher depreciation from the plants going on and potentially higher O&M? And I believe Rio goes in in 2013 and, I guess, Montana towards the end of the year. So mainly it's, I guess, depreciation with the units.

David Carpenter: Right. I don't know that it's going to completely offset the Rio 9 plant. You also have sales growth during that period that will help pay for Rio 9. But once Rio 9's completed, not only will you CWIP, you cease accruing the AFUDC, but you will also begin accruing depreciation. And so at this time we expect that you'll see a little bit of a decline in our earnings, or at least, maybe not earnings, but in our return in 2014 compared to 2013.

Anthony Crowdell: And just what is your assumption for the Palo Verde 3, the unregulated portion, in 2013 guidance?

David Carpenter: Say that again.

Anthony Crowdell: What's your assumption for the Palo Verde 3 unregulated - what's your subject for the contribution in 2013 guidance?

Steve Busser: Anthony, we're looking at probably about a 15 to 20 percent increase in terms of Palo Verde 3 contribution to pre-tax earnings in 2013 compared to 2012. In 2012 we had pre-tax earnings on Palo Verde of about $9.8 million. So that would be the base for the 15 to 20 percent increase that I just mentioned.

And I think the big driving factor there is just the gas price assumption. In 2012 we saw actual gas prices in the $2.75 range and our projected earnings that David went through in terms of earnings guidance for 2013 assumes a $3.50 gas price. Just to put that in perspective for you.

Mike Klein: Mike Klein, Sidoti. In the $0.18 benefit in your earnings bridge, can you just talk about the assumptions that go into the underlying growth? Maybe low growth or population growth or anything else that goes to that?

David Carpenter: Right, basically the revenue growth is about a 2.2 percent increase in revenue, excluding the effects of weather and the rate decrease. So maybe a little slightly less than we predicted in the past, but still a fairly positive. And we continue to be in that 2 to 3 percent range overall.

Mike Klein: Okay, and with the CAPEX outlook, can you just touch upon, going back to the markets in terms of raising additional equity?

David Carpenter: Right now our goal is to avoid going to the markets to issue equity. It's possible that we could have to issue equity in the future, but what we're seeking to do is to manage the needed equity for our capital construction program through kind of earnings and management of our dividend. And if we go to the equity market, I think it would be fairly, made a fairly small issue.

Steve Busser: Any other questions from anybody in the room?

Anthony Crowdell: Anthony Crowdell, Jeffries. Just on the AFUDC rate of 8.5 percent, do you get that on the total CWIP balance or haircut the CWIP balance that you're allowed that to?

David Carpenter: Right, there's standards for what projects you can accrue it on. You can't accrue it on projects that are under 30 days. And so, I think kind of our rule of thumb is, excluding the generation plant, we probably accrue AFUDC on about 85 percent of our plant. And then we accrue it on about 100 percent. Well, we don't accrue it on 100 percent of the generation plant additions. Fair enough?

Steve Busser: That's correct.

Maury May: its Maury May again of Wellington Shields. Just one more question on the rate base as it grows over the next five years. This allocation, of 75/25 between Texas and New Mexico that we've, you know that I've traditionally used. How does that shift by the end of the five year CAPEX program? Does it shift to like 80/20 or 82/18 or how do I allocate rate base between your two states going forward, next five years?

David Carpenter: Well, you have a little bit different situation now, Maury than you've had in the past, in that we've added about 50 megawatts of solar capacity in New Mexico. Now, that solar capacity attribution that it actually provides at the time of peak demand is about 65 to 70 percent of the total 47 megawatts.

And so that gets allocated to New Mexico first and then the remaining portion is split between Texas and New Mexico, and then I think if you look at the remaining portion, that it's probably in the 21 to 2 percent range for New Mexico and 78 percent or so for Texas. Does that sound right to you?

Steve Busser: Yes, a small sliver for FERC but not much.

Maury May: Now what was your investment in solar?

David Carpenter: It's all purchased solar so it's being recovered through our fuel factory in New Mexico.

Maury May: Okay, so what you're saying is on the rate base, you know, we're looking more of 78/22 split, going forward.

David Carpenter: That's correct.

Steve Busser: Anymore questions in the room? Dana, at this point if there are any questions for folks on the telephone, we'll go ahead and take those as well.

Operator: Thank you. If you'd like to ask a question on the phone please signal by pressing star 1 on your telephone keypad. If you're using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, that's star 1 to ask a question on the phone at this time. Sir, it appears we have no questions on the phone at this time.

Steve Busser: Okay, Dana, thank you.

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